

Summary of Business Rules for Accounting for and Reporting of Military Equipment

Modifications, Modernizations, Upgrades, and Improvements

Objective

- Provide guidance on accounting for and reporting of the cost of modifications that (1) extend the useful life of an end item or (2) enlarge or improve the capacity of an end item in accordance with Statement of Federal Financial Accounting Standards No. 6, *Accounting for Property, Plant, and Equipment*.

Baseline Valuation Methodology

- When modifications can be linked to individual end items:
 - The full cost of modifications that extend the useful life of an end item should be added to its net book value and depreciated over the end item's new useful life.
 - The cost of modifications that enlarge or improve the capacity of an item but do not extend its useful life should be capitalized by:
 - Adding the modification cost to the end item's net book value and depreciating the resulting cost over the remaining useful life of the end item, or
 - Capitalizing the modification as a separate item and depreciating the modification over the lesser of the life of the modification or the remaining useful life of the end item.
- In instances where modifications cannot be specifically identified with individual end items, the modification costs incurred during a given fiscal year should be aggregated, capitalized, and depreciated as a separate item. In addition, wherever possible, an estimate of the portion of these modification costs that is allocable to each item to which the modifications relate will be developed.
- Program managers will be asked to provide reasonable estimates of the useful lives of modifications, based on engineering estimates, prior experience, or other factors.
- When an end item is disposed of, both its remaining Net Book Value and the remaining Net Book Value of the related modifications will be written off.
- At times, modifications cross different acquisition programs, e.g., the same modifications may be applied to multiple types of aircraft. If it is impractical to specifically allocate the

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modifications to the programs or parent end items to which they apply, there will be no attempt to associate the modification cost with individual end items. In these situations, no adjustment will be made to the cost of modifications when the parent end item is disposed of, unless extraordinary losses of the related end items occur.

Mid-Term Valuation Methodology

- The full cost of modifications that extend the useful life of an end item should be added to its net book value and depreciated over the end item's new useful life.
- The cost of modifications that enlarge or improve the capacity of an item but do not extend its useful life should be capitalized by:
 - Adding the modification cost to the end item's net book value and depreciating the resulting cost over the remaining useful life of the end item, or
 - Capitalizing the modification as a separate item and depreciating the modification over the lesser of the life of the modification or the remaining useful life of the end item.